F I S C A L   I M P A C T   R E P O R T

		ORIGINAL DATE	2/16/19		
SPONSOR	Cadena/Trujillo, J.	**LAST UPDATED**		**HB**	515
SHORT TITLE	Child Care Assistance Gross Receipts			**SB**	
				ANALYST	Iglesias

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY19	FY20	FY21	FY22	FY23		
$0.0	(6,490.0)	(6,845.0)	(7,220.0)	(7,615.0)	Recurring	General Fund
$0.0	(4,100.0)	(4,325.0)	(4,560.0)	(4,810.0)	Recurring	Local Governments
$0.0	**(10,590.0)**	**(11,170.0)**	**(11,780.0)**	**(12,430.0)**	**Recurring**	**TOTAL**

Parenthesis ( ) indicate revenue decreases

Relates to HB160 and HB399

SOURCES OF INFORMATION
LFC Files

SUMMARY

Synopsis of Bill

House Bill 515 creates a new gross receipts tax (GRT) deduction for childcare assistance services contracted by the Children, Youth and Families Department (CYFD). The bill requires separate reporting for the deduction and requires the Taxation and Revenue Department (TRD) to compile an annual report for presentation to interim committees. The effective date of this bill July 1, 2019.

FISCAL IMPLICATIONS

The fiscal impact estimate uses data on childcare assistance funding sources and uses as documented in LFC's 2019 Volume III document.[1] In FY18, actual spending for childcare services was $133.5 million. The FY19 operating budget for childcare services is $139 million, and the LFC recommendation for FY20 is $148.5 million. Since this represents the amount spent on the licensed childcare assistance program, through which this bill proposes a deduction for

[1] Legislative Finance Committee, January 2019 for Fiscal Year 2020, Volume III, page 98, https://www.nmlegis.gov/Entity/LFC/Documents/Session_Publications/Budget_Recommendations/2020RecommendVolIII.pdf

those services, the estimate multiplies this amount by the FY19 year-to-date total statewide average GRT rate of 7.13 percent to arrive at a total cost of $10.6 million in FY20. The estimate assumes a 5 percent average annual growth rate for each fiscal year thereafter. Since the bill proposes a deduction for childcare services, gross receipts will be reduced for the state and local governments, and the estimate uses current average effective rates to apportion the cost between the two.

Because childcare assistance provider rates are set by formula (Section 8.15.2.17 NMAC), there would be no cost savings to CYFD for the deduction, as providers are currently unable to pass on the tax burden to the agency.[2] Therefore, licensed providers participating the childcare assistance program would realize the full benefit of the deduction.

This bill narrows the gross receipts tax (GRT) base. See *Significant Issues* for more information.

This bill may be counter to the LFC tax policy principle of adequacy, efficiency, and equity. Due to the increasing cost of tax expenditures, revenues may be insufficient to cover growing recurring appropriations.

Estimating the cost of tax expenditures is difficult. Confidentiality requirements surrounding certain taxpayer information create uncertainty, and analysts must frequently interpret third-party data sources. The statutory criteria for a tax expenditure may be ambiguous, further complicating the initial cost estimate of the expenditure's fiscal impact. Once a tax expenditure has been approved, information constraints continue to create challenges in tracking the real costs (and benefits) of tax expenditures.

SIGNIFICANT ISSUES

The Childcare Assistance program is a subsidy program for families with children between the ages of 3 weeks and 13 years whose families make less than 200 percent of the federal poverty level and who work or attend training and education programs. Aside from income eligibility requirements, parents must also work or go to school. The vast majority of qualified parents use childcare assistance to support their employment.

Childcare is not an entitlement program and is funded through a combination of federal block grants (Childcare and Development Fund, and Temporary Assistance for Needy Families) and state appropriations (general fund). Historically, the largest source of funding for childcare assistance was from the federal Childcare and Development Fund (CCDF), however, in FY19, the general fund has become the largest source of funding.

The bill does not include a purpose statement for the deduction; therefore, it is difficult to determine the bill's intended goal. The childcare assistance program already assists low-income families by covering costs of childcare; therefore, the childcare providers would receive the benefit of the deduction. The purpose of the deduction may be to provide tax parity among various providers of these services. Currently, for-profit childcare providers are subject to GRT, while similar services provided through the Public Education Department (such as afterschool

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[2] Legislative Finance Committee, January 2019 for Fiscal Year 2020, Volume III, page 99. Formula for provider reimbursement rates: (Base Rate + Quality Differential) x Units of Service = Provider Rate. Additional differentials to the provider rate apply for non-traditional work hours.

programs and prekindergarten) or by nonprofit providers receive the same provider reimbursement rates but are not subject to GRT.

Enrollment in childcare has growth the last three years, and CYFD projects continued growth in enrollment and costs. In FY18 childcare assistance average monthly enrollment was 20,488, an increase of 9.5 percent over FY17. The average monthly cost per child was $550, $53 more per child per month than FY17. Total direct spending for childcare assistance in FY18 was nearly $19 million above anticipated spending in CYFD's FY18 operating budget. In FY19, childcare assistance received an additional $22 million from the general fund and $3 million from TANF.

Increased provider rates for the highest levels of quality care contributed to increased spending as more providers qualify for 5-STAR reimbursements. Childcare providers can qualify as a 5-STAR provider by either meeting quality standards in the state's tiered rating quality improvement system, Focus, or through an approved national accrediting body. Periodically, the state recertifies childcare providers to ensure they are meeting Focus standards, while accredited providers are endorsed by their accrediting body.

This bill narrows the gross receipts tax (GRT) base. Many of the efforts over the last few years to reform New Mexico's taxes focused on broadening the GRT base and lowering the rates. Narrowing the base leads to continually rising GRT rates, increasing volatility in the state's largest general fund revenue source. Higher rates compound tax pyramiding issues and force consumers and businesses to pay higher taxes on all other purchases without an exemption, deduction, or credit.

PERFORMANCE IMPLICATIONS

The LFC tax policy of accountability is met with the bill's requirement to report annually to an interim legislative committee regarding the data compiled from the reports from taxpayers taking the deduction and other information to determine whether the deduction is meeting its purpose.

TECHNICAL ISSUES

This bill does not contain a delayed repeal date. LFC recommends adding a delayed repeal date.

Does the bill meet the Legislative Finance Committee tax policy principles?

1. **Adequacy**: Revenue should be adequate to fund needed government services.
2. **Efficiency**: Tax base should be as broad as possible and avoid excess reliance on one tax.
3. **Equity**: Different taxpayers should be treated fairly.
4. **Simplicity**: Collection should be simple and easily understood.
5. **Accountability**: Preferences should be easy to monitor and evaluate

Does the bill meet the Legislative Finance Committee tax expenditure policy principles?

1. **Vetted**: The proposed new or expanded tax expenditure was vetted through interim legislative committees, such as LFC and the Revenue Stabilization and Tax Policy Committee (RSTP), to review fiscal, legal, and general policy parameters.
2. **Targeted**: The tax expenditure has a clearly stated purpose, long-term goals, and measurable annual targets designed to mark progress toward the goals.
3. **Transparent**: The tax expenditure requires at least annual reporting by the recipients, the Taxation and Revenue Department, and other relevant agencies.
4. **Accountable**: The required reporting allows for analysis by members of the public to determine progress toward annual targets and determination of effectiveness and efficiency. The tax expenditure is set to expire unless legislative action is taken to review the tax expenditure and extend the expiration date.
5. **Effective**: The tax expenditure fulfills the stated purpose. If the tax expenditure is designed to alter behavior – for example, economic development incentives intended to increase economic growth – there are indicators the recipients would not have performed the desired actions "but for" the existence of the tax expenditure.
6. **Efficient:** The tax expenditure is the most cost-effective way to achieve the desired results.

LFC Tax Expenditure Policy Principle	Met?	Comments
Vetted	✘	Not heard in an interim committee of LFC or RSTP.
Targeted		
Clearly stated purpose	✘	No stated purpose.
Long-term goals	✘	None.
Measurable targets	✘	None.
Transparent	✓	Bill requires to TRD to compile an annual report on the deduction, including the aggregate amount of deductions claimed and number of taxpayers claiming the deduction, and the department is to report a cost analysis to RSTP and LFC.
Accountable		
Public analysis	?	Because there is no stated purpose, it is indeterminate whether reporting on the number of taxpayers and cost of deduction is sufficient for public analysis on the effectiveness of the deduction.
Expiration date	✘	Bill does not contain a delayed repeal date. LFC recommends adding a delayed repeal date.
Effective		
Fulfills stated purpose	?	No stated purpose.
Passes "but for" test	?	
Efficient	?	Because there is no stated purpose, staff cannot determine if this deduction is the most cost-effective way to achieve the desired results.
Key: ✓ Met ✘ Not Met ? Unclear		

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